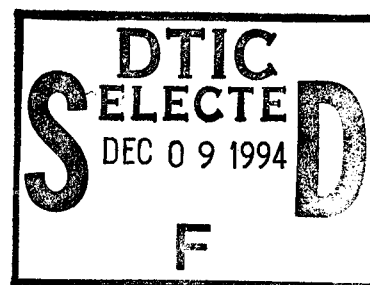


1994
Executive Research Project
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Paying the Bills of a Major Program: An Alternative Approach



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The Industrial College of the Armed Forces
National Defense University
Fort McNair, Washington, D.C. 20319-6000

19941201 094

REPORT DOCUMENTATION PAGE

1a. REPORT SECURITY CLASSIFICATION Unclassified		1b. RESTRICTIVE MARKINGS	
2a. SECURITY CLASSIFICATION AUTHORITY N/A		3. DISTRIBUTION/AVAILABILITY OF REPORT Distribution Statement A: Approved for public release; distribution is unlimited.	
2b. DECLASSIFICATION/DOWNGRADING SCHEDULE N/A		5. MONITORING ORGANIZATION REPORT NUMBER(S) Same	
4. PERFORMING ORGANIZATION REPORT NUMBER(S) NDU-ICAF-94-21		7a. NAME OF MONITORING ORGANIZATION National Defense University	
6a. NAME OF PERFORMING ORGANIZATION Industrial College of the Armed Forces	6b. OFFICE SYMBOL (If applicable) ICAF-FAP	7b. ADDRESS (City, State, and ZIP Code) Fort Lesley J. McNair Washington, D.C. 20319-6000	
6c. ADDRESS (City, State, and ZIP Code) Fort Lesley J. McNair Washington, D.C. 20319-6000	8b. OFFICE SYMBOL (If applicable)	9. PROCUREMENT INSTRUMENT IDENTIFICATION NUMBER	
8a. NAME OF FUNDING/SPONSORING ORGANIZATION	8c. ADDRESS (City, State, and ZIP Code)	10. SOURCE OF FUNDING NUMBERS	
		PROGRAM ELEMENT NO.	TASK NO.
		PROJECT NO.	WORK UNIT ACCESSION NO.
11. TITLE (Include Security Classification) <i>Playing the Bills of A Major Program: An Alternative Approach.</i>			
12. PERSONAL AUTHOR(S) <i>Jerry Backlund</i>			
13a. TYPE OF REPORT Research	13b. TIME COVERED FROM <i>Aug 93</i> TO <i>Apr 94</i>	14. DATE OF REPORT (Year, Month, Day) April 1994	15. PAGE COUNT <i>31</i>
16. SUPPLEMENTARY NOTATION			
17. COSATI CODES		18. SUBJECT TERMS (Continue on reverse if necessary and identify by block number)	
FIELD	GROUP	SUB-GROUP	
19. ABSTRACT (Continue on reverse if necessary and identify by block number)			
SEE ATTACHED			
20. DISTRIBUTION/AVAILABILITY OF ABSTRACT <input checked="" type="checkbox"/> UNCLASSIFIED/UNLIMITED <input checked="" type="checkbox"/> SAME AS RPT. <input type="checkbox"/> DTIC USERS		21. ABSTRACT SECURITY CLASSIFICATION Unclassified	
22a. NAME OF RESPONSIBLE INDIVIDUAL Judy Clark		22b. TELEPHONE (Include Area Code) (202) 475-1889	22c. OFFICE SYMBOL ICAF-FAP

PAYING THE BILLS OF A MAJOR PROGRAM: AN ALTERNATIVE APPROACH

ABSTRACT

This research paper analyzes the feasibility of using commercial banking practices and Electronic Data Interchange (EDI) in paying bills. The information revolution requires technology that the United States Government cannot afford to purchase, maintain and update in accomplishing normal finance and accounting business practices. Technology is moving too quickly. In order to take advantage of the information revolution, business practices need to be reengineered not just automated. With the current downsizing of the Armed Forces and with the commercially available computer and information capabilities, it is time to explore new and innovative approaches to paying bills for our major programs. The way we do business is changing due to the impact of the computer and the exchange of electronic information.

JERRY A. BACKLUND

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I. INTRODUCTION

A. BACKGROUND

The ability to reinvent government provides challenges and opportunities to be innovative and to take advantage of the latest technologies, best business practices, and other streamlining techniques allowing government to pursue its missions in the most effective ways possible. The measurement for reinventing government was outlined in the Report of the National Performance Review by Vice President Al Gore on Sep 7, 1993:

We will invent a government that puts people first, by:

- Cutting unnecessary spending...
- Empowering its employees...
- Fostering excellence

Here's how. We will:...

- Steer more, row less
- Delegate authority and responsibility...
- Search for market, not administrative, solutions....(Gore, 1993).

Current efforts to reinvent government include acquisition reform. The acquisition community must not only work with less but also needs to reengineer work processes. One area which provides opportunities for process improvement, cost reduction, and increased customer satisfaction is the method the government uses to pay bills on major weapon system contracts. Advancements in Information Technology offer revolutionary techniques that are currently being utilized in the commercial sectors.

B. OBJECTIVE AND SCOPE

The objective of this research is to (1) examine the processes currently being used to pay bills on major weapon systems contracts; (2) analyze the concerns with these processes from the point of view of program managers, contractors, and financial managers; (3) discuss the costs of the current processes; and (4) investigate contracting out the process to take advantage of the current electronic commercial marketplace.

C. METHODOLOGY

The methodology for this research consisted primarily of reviews of existing laws; interviews with current program managers, prior program managers, contractors, financial officers, Headquarters-level managers, and banking officers; and reviews of other research publications and articles on acquisition reform. An initial search for relevant current data did not reveal details of processes being used by program managers and financial offices. Since current information on this topic was not readily available, interviews were the best source of information. The questions asked were stated to be non-leading and neutral in nature. Interviews were conducted with program managers, contractor project managers, and government financial experts (all with experience on major acquisition programs). Most of the contractor project managers were previously involved in the acquisition process as military officers. Additional information was obtained through telephone interviews with personnel from American Express and the Defense Financial Accounting Service (DFAS). Military Service and Office of Secretary of Defense (OSD) level perspectives were researched by reviewing papers written from a Military

Service perspective, by interviewing personnel from major OSD programs and individual Service programs, and by reviewing briefings/presentations made by Service financial experts. Questions asked were as follows:

FOR GOVERNMENT MANAGERS:

1. Would contracting out to a "bank-type" contractor for payment transactions provide you with the accounting data you require?
2. If yes, What type of information and what frequency of data do you require/like to have?
3. Would you have confidence in a "debit card-type" accounting system?
4. Even with the Prompt Payment Act, is timely payment of bills still a problem?
5. Any other issues/comments?

FOR CONTRACTOR PROJECT MANAGERS:

1. Would prompt payment of government bills increase your efficiency?
2. Would contractors currently not bidding on government contracts bid if they knew payments would be more prompt?
3. Would electronic transfer of funds cause a change in your accounting costs?
4. Any other issues/comments?

D. RESEARCH PAPER ORGANIZATION

Chapter II discusses current legal issues. It reviews the current acquisition and accounting processes. It also reviews the issues and concerns with those processes as divulged by government program managers and financial experts and contractors.

Chapter III discloses the costs associated with the current processes to include current costs and future costs. This includes the cost of automation upgrades and manpower costs. Also commercial disbursement services are discussed including some documented results on the cost of processing vouchers in the commercial sector. Additionally discussed are the costs involved in the loss of confidence in the public sector by both the American public and the Congress.

Chapter IV provides a brief summary, draws conclusions and provides a recommendation for process improvement through the implementation of a demonstration debit card program. An example of how the debit card program could work is explained and compared to how individuals conduct their personal business.

II. CURRENT ISSUES

A. LEGAL ISSUES

The Prompt Payment Act of 1982 required Federal Agencies to pay their bills in a timely manner or to pay interest on those bills paid late (Prompt Payment Act of 1982). It also stated that Federal agencies would take early payment discounts when payments were paid within the discount period. The Prompt Payment Act and subsequent regulations also allowed for electronic payment of bills, to include FAST PAY (Federal Acquisition Regulation, Section 13.3). FAST PAY is used to expedite payment for small purchases. According to Mark E. Romanoff, who has been employed by the Department of Defense at Fort Meade, MD as Business Manager and in a staff assignment overseeing the business management function, the FAST PAY process would be appropriate for repetitive transactions (Romanoff, 1990). In interviews, some government program managers reported that major contract invoices were not being paid on time, while others said only the smaller contracts were not being paid in a timely manner despite the Prompt Payment Act. Although the high dollar amounts being paid in these program offices were for the larger contracts, the program offices also must track expenditures for smaller contracts.

B. THE CURRENT PROCESS

The process seems simple enough. An order or contract is issued; the procured item is received; an invoice is submitted for payment; and finally, the bill is paid. A four step process that is not as simple as it appears.

A closer look shows the following: (1) a program office acquires systems through contracts; (2) these contracts are usually administered by the Defense Logistics Agency (DLA) and paid by the Defense Finance and Accounting Service (DFAS); (3) after the government accepts items required by the contracts, the contractor submits an invoice to DFAS; (4) the payment of the invoice must comply with the Prompt Payment Act and Cash Management Policies which state that the government should hold the invoice until the last day possible without incurring Prompt Payment Act penalties; and (5) payments are often late, inaccurate, involve penalties and result in high overhead costs for both the government and contractors. Other problems are caused by the paying office not being located at the same place as the office receiving the purchased item or even the office issuing the contract. The paying office must wait until it receives reports through its accounting records with these reports matching exactly the invoices received. If they don't match, they are researched and/or returned (Defense Logistics Agency, 1984). Office of Management and Budget (OMB) requires agencies to cite from a list of ten reasons why a penalty was incurred for late payment. These reasons are: (1) contract not available in payment office, (2) delay in receiving documentation, (3) delay in certification of invoice, (4) delay by payment office, (5) military exercise in progress, (6) discount taken in error, (7) vendor not notified of defective invoice within fifteen days, (8) automated system processing delay, (9) delay caused by U. S. Postal Service, and (10) other (Assistant Secretary of Defense (Comptroller) memorandum, 1982).

Currently invoices are submitted to DFAS at Columbus, Ohio (with the exception of 6,000 Air Force contracts that are currently processed at Albuquerque, New Mexico. These contracts will be transferred to the Columbus location within the next year.). The Columbus Center currently

employs about 3300 people. The consolidation of work to the Columbus Center began in May, 1989 with the latest transfer in November, 1992. The only transfer left is the Albuquerque Office. The Columbus Center is still hiring and, although turnover outside the organization is not a problem, there is tremendous movement within the organization. The average journeyman position is GS-6 level with supervisors and experts slightly higher. Most new hires are at the GS-4 (salary \$16,393 - \$21,307 per annum) target GS-5 (salary \$18,340 - \$23,839 per annum) or GS-6 (salary \$20,443 - \$26,572 per annum) level. Officials at the Columbus Center felt that it will be another one and a half years before they are up to strength. When asked if the Center had a unit cost of processing contract invoices, officials stated that there is no good measurement at this time due to the consolidation effort and movement within the organization. In anticipation of the Albuquerque transfer, some positions are being double staffed so that employees can be trained properly before the move. They seem to be doing everything the system will allow to make an efficient and effective transfer. However, the system remains a barrier. Computers are a mix of everything from Zenith-248's transferred from the old offices to newly purchased 486 DOS machines. The computer systems currently being used are MOCAS (Mechanization Of Contract Administration Service), a DOD financial system for administering and paying contracts; AMIS (Acquisition Management Information System), an AF procurement system providing financial data on all central procurement contracts used at the Albuquerque office; and others. DFAS has developed front-end interfaces for MOCAS but the software is being changed even as the interfaces are developed. DFAS is experiencing the same resource difficulties as the rest of DOD. Funding is insufficient to purchase all of the needed new equipment and

software; many of the employees are still in the developmental stage of their expertise; and finally the procurement process doesn't move fast enough.

The program offices are still keeping their own accounting books so that they can reconcile expenditure status information with the DFAS reports. This requires extensive staff work for both the program office and the contractor. Most program offices at all levels in DOD stated that most corrections required multiple submissions before the error was corrected. Costs for each invoice are measured not only in the cost of DFAS personnel but in the additional costs for the program offices, the comptroller offices, and the contractors in tracking the most accurate and timely data available.

C. PROGRAM MANAGERS' ISSUES

The first and foremost issue discussed by the government program managers was the *timeliness* and *accuracy* of the expenditure data provided by the current systems and processes. Each major program office has a financial team that spends much of its time reconciling errors in the accounting system and then inputting the corrections into the system so that reports to headquarters, OSD and Congress reflect accurate program execution. Due to the process involved, accurate data is not timely.

An overview of the process appears simple enough—a contractor sends an invoice to the government and the government pays it. Unfortunately, things are rarely that simple. Contractors often forget to include purchase order numbers or contract numbers on invoices or they provide descriptions that differ from items listed in the contract. These invoices must be returned to the contractors or the errors corrected within fifteen days in order to stop the countdown for Prompt Payment Act violations (OMB Circular Number A-125).

Even when invoices are submitted correctly, the process may break down. Accounting clerks, who have stacks of invoices to process, may charge these invoices to the wrong appropriations or to the wrong fiscal year account, transpose numbers when entering the data, or place an invoice aside because there is no clear match to a contract or account. The program managers interviewed felt strongly that the accounting personnel are doing the best they can but that they lack the expertise and detailed knowledge of the contract and program specific execution insight. This process, unfortunately, provides the program manager, higher headquarters, OSD, and the Congress with program execution data that is inaccurate and untimely. Several of these program managers had had their programs reduced based on expenditure data that was incorrect.

The second most recurring issue concerned the time and resources that the program office had to dedicate to duplicate bookkeeping and error correction. All the program managers interviewed felt that their staffs spend too much time correcting errors in the finance and accounting process. According to one briefing on Contract Financial Reconciliation dated 6 December 1993, correct expenditure status is not being maintained (SMC/FM Briefing, Dec 1993). The Defense Financial Accounting Service (DFAS) expenditure system is complex; expenditures are critical to program managers yet they have little insight. The briefing recommended that the program offices track expenditures by obtaining invoice information from the contractor or the contract administrator. Resulting reports would be used to provide the program manager with current expenditure status and would be used to verify and/or correct DFAS records.

Other concerns discussed involved violations due to invoices being charged against the wrong accounts, interest penalties due to payment delay

and the inconsistent expenditure data being generated by the process but being used by higher headquarters, OSD, OMB and Congress in making programmatic decisions (SMC/FM Briefing, Dec 1993). This briefing confirms the information obtained from the program managers that keeping a backup set of books to the official system is essential in managing a program.

D. CONTRACTOR PROJECT MANAGERS' ISSUES

The Contractor project managers voiced concerns about prompt payment and the difficulty in providing all the invoice information "in the right format". All of the small business contractors stated that cash flow is critical to their doing business. If they have to borrow money to cover outlays, their costs increase. The cost is then passed on to their client—in this case, the program office. Other small business project managers said that they just can't afford to do business with the government. The small business project managers aren't the only ones not able to afford to do business with the government. With the current downsizing and restructuring of the defense industry (General Electric sold its Aerospace plant; General Dynamics sold or is in the process of selling its Fort Worth, Electronics, Missiles, and Cessna plants. And others are selling their defense divisions.) there will be fewer prime contractors in the defense business. The bottom line is that there are and will be in the future fewer government contracts. Cash flow and timely payments are critical to all contractors in this environment.

Another area of concern to all of the contractor project managers was the extensive paperwork required to do business with the government. In order to meet government requirements, contractors must comply with complex finance and accounting practices so that specific government reports can be generated.

Additionally, staff must work with the government program office staff to ensure the government expenditure data is accurate and timely. Multiple copies of documents have to be sent to different government offices.

III. POTENTIAL IMPACTS

A. AUTOMATION UPGRADES

The cost of upgrading computers is only a small part of the cost of automation. A personal computer (PC) with its related software and peripherals can be purchased for around \$3,000. The cost of the computer is then multiplied by the number of employees needing the computer. As new technology is developed, old computers need to be upgraded to take advantage of the newer capabilities. The federal government has difficulty keeping up. This is especially true in the cases of supporting activities who provide finance and accounting services rather than building new weapons systems. These support activities do not always receive the funding necessary to buy this equipment nor do they receive the waivers for streamlined procurement.

Automation, however, is not simply buying new computers, software, and peripheral equipment. What is really needed is to reengineer the complete process instead of computerizing the old processes. Opportunities are being missed. These offices need to rethink their processes and reengineer them while taking advantage of the information technology that's available. DFAS and other government accounting offices are continuing to computerize old processes because they can't afford to stop everything and start anew.

B. EDI CAPABILITIES

Electronic Data Interchange (EDI) is the electronic exchange of formatted business transactions between one organization's computer and another organization's computer. Many have advocated EDI as the computer

technology that holds the greatest potential for improving the nation's productivity bringing both private and public sector businesses to a paperless environment—one based solely on electronic transactions. EDI can be used to support transactions that are well-defined and redundant. The EDI process requires that each transaction be formatted in such a way that it is recognized by an organization's computer without the need for a person to interpret the transaction for the computer (American National Standards Institute).

As with any new technology, EDI requires a reengineering of processes and, in this case, an infrastructure that can support it. The infrastructure linking computers and the defined formats can be the first tracks of the information highway linking offices across the country. The use of EDI in the private sector has steadily increased after its introduction in the late 1960's. It has matured to the point that many spin-off capabilities are now arriving on the scene.

C. COMMERCIAL DISBURSEMENT SERVICES

One of the spin-off capabilities from EDI technology is a new commercially available disbursement service offered by American Express in January, 1994. According to Ms. Christine Levite, Director of Public Affairs for American Express, American Express contracted Ernst & Young to do a survey on the costs of purchasing supplies, equipment, and services by large U. S. corporations (Levite Telephone Interview, 1994). American Express's goal was to unveil a new corporate purchasing card and to become known as business expense management experts (Levite, 1994). In January, 1994, they made their announcement reflecting the results of a year-long pilot program. Ten

U. S. corporations took part in the pilot program, including IBM, Scott Paper Company and Northrop Corporation. They documented that the purchase order process is labor and paper-intensive. Scott Paper Company estimated that it cost an average of \$152 to process a single transaction. By using an American Express purchasing card, they lowered the cost to \$3 per transaction. IBM found savings too—from \$50-\$100 to \$1 per transaction (Levite, 1994). Whether using a purchasing card or a bank debit card, the savings would be the same. Companies that participated in the pilot found improved vendor management in terms of sourcing, prompt pay and improved relationships; reduction in accounting and processing, to include purchasing cycle time, manpower, and cost; and better financial control. The database showed that these are areas of interest in non-manufacturing, manufacturing, and aircraft/defense industries alike.

D. FUTURE MANPOWER

The Department of Defense is facing major manpower reductions. It can no longer afford to computerize; it needs to automate. Processes need to be reengineered. The concept of Integrated Product Teams (IPT's) is becoming key in management philosophy today (White Paper, 1993). In terms of a program office the IPT is responsible and accountable for all processes assigned to the team. This includes activities such as engineering design, logistic support, financing, contracting, producibility, integrated requirements, etc. (AFMCP 800-60 (C1).1993). In other words all functions are represented on a team having a common purpose and holding themselves mutually accountable. In order to create an IPT, the process involved needs to be defined so that appropriate team members are selected. Defining the process is the first step

in reengineering their processes so that they can take advantage of automation, not just computerize.

Dr. William Perry, the current Secretary of Defense, in an interview in October, 1993, stated that in the financial management area the consolidation proposed in previous government reviews might not be the most efficient (Perry, October 1993). IPT's, if given the standardized tools Dr. Perry discussed, have the expertise and "pride of ownership" to be the most efficient. The standardized tools could be those already used in the banking industry instead of choosing a system from among the various government agencies and military services. Then the financial tracking could be contracted out to the commercial sector.

E. LOST CONFIDENCE

Newspaper articles frequently are published about perceived waste and mismanagement in the federal government. Whether or not these accounts are accurate is irrelevant. Acquisition reform is a popular topic because the American public and Congress believe DOD doesn't manage as efficiently as it could. Many of the stories about expensive toilet seats, hammers, or fruitcakes are often based upon cost accounting that includes legitimate overhead costs and costs of special accounting requirements (Gansler, 1989). In addition, the newspapers are also filled with stories of cost overruns and either mismanagement or at least "poor judgment" on the part of government managers. Congress receives execution status reports and sees that a program is not executing the current year dollars and cuts or cancels that program's appropriation and/or authorization. OSD will sometimes cut programs for the same reason, even if Congress doesn't. Unfortunately, many of the execution

reports are, as discussed earlier, untimely and inaccurate. Acquisition reform will hopefully address some of the special accounting requirements that make costs look so absurd, but the current financial reporting system will always be too late to answer management questions necessary for the program manager, OSD, and Congress.

IV. SUMMARY, CONCLUSIONS, AND RECOMMENDATIONS

There are ways the government can improve the process for paying the bills of major acquisition programs and there are many different solutions that could work to some degree. When those individuals who have the most to gain by getting work accomplished are given the authority and tools to do their work, it gets done right. Instead of centralizing finance and accounting functions at DFAS, why not let selected program offices manage their accounts like a business by authorizing a demonstration debit card program. Issue their funds to them, according to their disbursement plan, on a quarterly basis and let them pay their bills from their "checking account" with a commercial financial institution. The financial institution will pay the bills (as in the case of American Express in one to three days) once the debit is approved by the appropriate IPT member, just as we pay our personal bills for services rendered or purchases received. Specifically, the basic steps are: (1) OSD authorizes transfer of funds from the U. S. Treasury to the program office's commercial checking account quarterly; (2) as bills are received and validated by the program office, they send electronic notice to the commercial financial institution to transfer specific amounts to the contractor; and (3) the commercial financial institution transfers the funds to the contractor electronically.

By using true automation, the bank and the program office would be electronically linked. The appropriate IPT members could have immediate access for viewing their account status. Those with actual approval authority could authorize payment electronically once the contractor submitted appropriate invoices, progress payment status, etc. Payment would be through

electronic transfer of funds to the contractor's banking account. There would be no checks printed or mailed. Monthly reports could be in the format requested by the program office and as defined at the time the account was established with the financial institution. All aspects of the management of the program would be vested with the program office. Spot audits could and should be conducted, just as in the commercial sector. Accounts could be established for different appropriations or fiscal year appropriations.

One of the financial managers interviewed has conducted extensive audits on various OSD major programs. He estimated that this process could result in a 5% - 7% savings on the overall cost of doing business in a program office. This includes savings in the program office by having to spend less time researching and correcting errors, by having to spend less time defending budget cuts when the funds are already spent, by having to spend less time ensuring execution reports to higher headquarters are accurate but also potentially having more contractors willing to bid on government contracts thereby increasing competition and reducing government costs.

This savings, however, is offset to some degree due to the fact that as the program office becomes more efficient in paying bills, dollars will be taken out of the U. S. Treasury faster. This loss of dollars from the treasury can additionally be offset to some degree by the fact that there are fewer major acquisition programs today will probably be fewer in the upcoming years. The slow process that we currently have has had the positive effect of slowing the removal of dollars from the treasury. Additionally, each program office IPT would be required to estimate their expenditures and update those if there were significant changes to their programs. These disbursement plans would be the basis for "deposits" into their checking account. The program managers interviewed agreed that quarterly deposits would probably be the most effective

time frame although monthly deposits would have the least effect on the treasury. Currently, program offices submit disbursement plans, but because the system has so many barriers to execution (especially in the processing of payments), they are often inaccurate. If the IPT has control of its processes and is given the tools necessary to function, accurate spend plans could be the norm.

There would also be substantial savings in reduced personnel costs. All program managers agreed that most of the individuals at DFAS are doing the best work they can but they lack the training and they especially lack the specific program office expertise to be able to match invoices to contracts quickly and correctly. It is simply not efficient to have to keep two sets of books as is being done now. As stated in the Contract Financial Reconciliation briefing, there is a critical need for program office contract reconciliation. The problem is complex. There are many obligation and expenditure reporting mistakes. Auditing can be very time-consuming. The cross-mapping can be tedious and lengthy. The entire process is further complicated by end of fiscal year "fire drill" efforts and by having no validated "check and balance" system. The recommended action was that the program office should maintain current obligation and expenditure status of all contracts (Contract Financial Reconciliation, 1993). The program office would need a standardized database model to track details and produce reports. This would provide for a near real-time obligation and expenditure status. The recommended action also stated that the database reports produced would be used to verify and correct all other government reports.

The best standardized database would be the one banks are currently using everyday. Commercial business practices are normally more efficient due to competitive market pressures. Money can be and is being transferred

around the world. Today's computer and electronic data exchange technology is making it even easier. An individual can pay their personal bills from home by computer using standardized software. They don't have to write a check. At ATM's across the country, a person can withdraw money, get current balance status, and transfer funds. Program Offices could do business the same way. The software and the interface with the financial institution would need to be somewhat more complex than for our individual accounts, but the security procedures and systems are already there—as is the basic concept. Credit cards are used by contracting officers in federal agencies to purchase small dollar value items—again mirroring how an individual makes small purchases and keeps track of small purchases in their personal business. The time is right to take the next step from credit card to debit card.

The information highway is ready for high speed transactions today. We must plan for the future when those not on the highway will be left behind. In our bureaucracy, we move slowly and many of us think that the speed will never change. It doesn't have to be that way. We have an opportunity to streamline our processes and maximize all of our resources. Resources that are quickly dissolving. Innovation and farsightedness are the tools that help us plan for the future. A future with expert teams managing their programs effectively and efficiently, using all their resources wisely while speeding down the information highway.

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